

Message Text

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AMEMBASSY DOHA

AMEMBASSY JAKARTA

AMEMBASSY JIDDA

AMEMBASSY KUWAIT

AMEMBASSY LONDON

AMEMBASSY QUITO

AMEMBASSY TRIPOLI

USMISSION EC BRUSSELS

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C O N F I D E N T I A L TEHRAN 8767

EXDIS

KUWAIT PASS DOHA

E.O. 11652: GDS

TAGS: ENRG, IR

SUBJ: SINGLE OIL PRICE

REF: TEHRAN 7611

1. SUMMARY: THIS CABLE ATTEMPTS TO EXPLAIN SHAH'S "SINGLE-PRICE" PROPOSAL AS METHOD OF ENDING WHAT PRODUCER GOVERNMENTS CONSIDER THE TROUBLESOME GAP THAT PERSISTS BETWEEN PRICES OF EQUITY CRUDE AND BUYBACK/GOVERNMENT MARKET CRUDE. THE FIGURE HE MENTIONED AS SINGLE PRICE IS \$9.845 PER BARREL, THE WEIGHTED AVERAGE COST OF ARABIAN LIGHT CRUDE SUPPOSEDLY IMPLIED BY THE SEPTEMBER OPEC PRICE INCREASE. SHAH APPARENTLY WOULD LIKE "SINGLE PRICES" OF ALL OTHER OPEC CRUDEs TO BE RELATED TO THE ABOVE FIGURE ON BASIS OF QUALITY AND FREIGHT DIFFERENTIALS. THERE IS SOME INDICATION HE

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RECOGNIZES USEFULNESS OF GIVING SLIGHT DISCOUNT OFF THIS PRICE TO

MAJOR COMPANIES WHO HAVE HELD CONCESSIONS IN EACH PRODUCING COUNTRY. SINGLE-PRICE IDEA SEEMS TO US PREFERABLE TO EXISTING CHAOS IN PRICING ARRANGEMENTS, BUT PROPOSED LEVEL IS VERY HIGH. WE FEEL CONSUMER/PRODUCER TALKS MUST BE HELD BEFORE THIS IDEA CATCHES ON AND HARDENS AT SO HIGH A LEVEL. END SUMMARY.

2. WE NOTE THAT NESA WIRELESS FILE NO 200, OCT 15, 1974, REPORTS AP DISPATCH FROM TEHRAN SAYING IRAN PROPOSED "FIXED OIL PRICE OF 9.84 PER BARREL" IN LIEU OF PRESENT PRICING SYSTEM. AP CITES KAYHAN AS SOURCE OF THIS REPORT. KAYHAN INTERNATIONAL OCT 15 EDITORIALIZED, UNDER TITLE "IRAN WON'T TOLERATE REDUCTION IN OIL PURCHASING POWER", THAT IN VIEW OF CERTAIN REPORTED SAUDI STATEMENTS ON OIL PRICES, IT IS IMPORTANT "TO RESTATE IRAN'S LOGICAL PROPOSAL CONCERNING THE PRICE OF OIL...THE SHAHANSHAH HAS PROPOSED THAT OIL SHOULD HAVE A SINGLE PRICE ONLY. IT SHOULD BE WORKED OUT ON THE BASIS OF THE 40-60 PERCENT PARTICIPATION SCHEME CURRENTLY ENFORCED IN KUWAIT. THIS WOULD MEAN THAT THE PRICE FOR MARKER CRUDE (IE ARABIAN LIGHT) IN THE PERSIAN GULF WOULD BE \$9.84 RPT \$9.84 PER BARREL."

3. MOST OF THE AP DISPATCH IS GARBLED AND SHOULD BE IGNORED. BACKGROUND TO SHAH'S PROPOSAL, OF COURSE, IS THAT OPEC'S RAPID INCREASES IN POSTED PRICES LATE LAST YEAR PLUS THE RAPID AND CONFUSED DEVELOPMENTS IN NEW PARTICIPATION AGREEMENTS CREATED TWO KINDS OF PRICES IN THE PERSIAN GULF: TAX-PAID-COST OF AROUND \$7 TO \$7.50 FOR THE MAJOR COMPANIES "EQUITY OIL" AND A GOVERNMENT MARKET/BUYBACK PRICE OF SOME \$10.80 TO OVER \$11.00 FOR THE 60 PERCENT GOVERNMENT SHARE. EFFECT OF THIS WIDE DISPARITY IN PRICE WAS TO ALLOW COMPANIES SEVERELY TO UNDERCUT GOVERNMENTS' DIRECT SALES BECAUSE OF LOWER COST TO THE COMPANIES -- AN AVERAGE, WEIGHTED BY THE VOLUME OF OIL, OF TAX-PAID-COST AND BUYBACK PRICES. RESULT IN KUWAIT, AS WE UNDERSTAND IT, WAS THAT KUWAIT'S ADHERENCE TO GOVERNMENT PRICE OF 94.846 PERCENT OF POSTED PRICE (\$10.95) FORCED GOK TO SHUT-IN SOME 500,000 B/D OF PRODUCTION THAT IT COULD NOT SELL, WHILE COMPANIES OBTAINED 1.7 MMB/D AT WEIGHTED AVERAGE COST OF AROUND \$8.68. (WE WONDER WHETHER GOK WILL SOON INSIST ON A RETROACTIVE "CORRECTION" OF THIS SITUATION).

4. CLEAR PURPOSE OF OPEC SEPTEMBER DECISION WAS TO NARROW GAP BETWEEN TAX-PAID-COST AND PRODUCER GOVERNMENT PRICE. THIS IS TO BE CONFIDENTIAL

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ACHIEVED (A) BY FIXING THE FOURTH QUARTER 1974 WEIGHTED AVERAGE GOVERNMENT TAKE PER BARREL AT 3.5 PERCENT ABOVE THE HYPOTHETICAL THIRD QUARTER LEVEL, (B) BY LOWERING THE GOVERNMENT SALES PRICE TO 93 PERCENT OF POSTED PRICES AND (C) BY APPLYING THE ENTIRE INCREASE (PLUS THE AMOUNT SUBTRACTED FROM THE GOVERNMENT SALES PRICE) TO THE COST OF THE COMPANIES EQUITY OIL. THEY "HYPOTHETICAL" THIRD QUARTER LEVEL OF GOVERNMENT TAKE WAS CALCULATED BY OPEC AS A WEIGHTED AVERAGE OF 40 PERCENT OF EXPORT CRUDE AT TAX PAID COST

(BASED ON ESTABLISHED POSTED PRICES, 14.5 PERCENT ROYALTY RATE AND 55 PERCENT INCOME TAX RATE) AND PLUS 60 PERCENT OF CRUDE AT GOVERNMENT PRICE OF 94.846 PERCENT OF POSTED PRICE. CALCULATIONS ON THIS BASIS WOULD GIVE, FOR ARABIAN LIGHT, A TAX-PAID COST OF \$8.360 (BASED ON UNCHANGED POSTED PRICE, 16.67 PERCENT ROYALTY, AND 65.75 PERCENT TAX RATE), A GOVERNMENT PRICE OF \$10.835, A WEIGHTED AVERAGE COST OF \$9.845, AND A WEIGHTED AVERAGE GOVERNMENT TAKE OF \$9.745 (BASED ON TEN CENT PRODUCTION COST). THUS GAP BETWEEN TAX PAID COST AND GOVERNMENT PRICE IS REDUCED BUT STILL LARGE.

5. SEEN AGAINST THIS BACKGROUND, SHAH'S SINGLE PRICE PROPOSAL MEANS "LET'S ELIMINATE THE GAP ENTIRELY BY ESTABLISHING ONE SINGLE PRICE FOR THE MERKER CRUDE, AND DERIVING SINGLE PRICES FOR OTHER GULF CRUDES FROM THAT PRICE BY APPLICATION OF THE PRESENT SULPHUR AND SPECIFIC GRAVITY DIFFERENTIALS. FURTHER, LET'S USE THE WEIGHTED AVERAGE COST OF ARABIAN LIGHT IMPLIED BY THE SEPTEMBER OPEC MEETING, THAT IS \$9.845 PER BARREL, AS A STARTING POINT." AS OUR PREVIOUS REPORTING HAS INDICATED, SHAH SEEMS TO RECOGNIZE NEED FOR SOME SLIGHT DISCOUNT OFF THIS PRICE FOR MAJOR COMPANIES (CONSORTIUM MEMBERS IN IRAN'S CASE) AND HE WOULD LIKE TO SEE PRICES OF ALL OPEC CRUDES RELATED TO THE SAME MARKET PRICE THROUGH GRAVITY, SULPHUR AND TRANSPORTATION DIFFERENTIALS.

6. OUR VIEW IS THAT IN PRINCIPLE A SINGLE-PRICE SYSTEM OF THIS SORT WOULD SURELY BE PREFERABLE TO PRESENT UTTER CHAOS IN PRICING ARRANGEMENTS, IN WHICH CHANGING AGREEMENTS ON BUYBACK PRICES AND VOLUMES CAUSE FREQUENT AND UNCERTAIN FLUCTUATIONS IN COSTS TO COMPANIES AND CONSUMER NATIONS. THE LEVEL PROPOSED BY THE SHAH (ON BASIS, WE NOTE, OF UNANIMOUS OPEC DECISION) IS EXTREMELY HIGH, AND WOULD IMPLY AN INCREASE OF MORE THAN ONE DOLLAR PER BARREL OVER PRESENT LEVEL OF CONSORTIUM MEMBERS' PAYMENTS TO IRAN. ON AN ANNUAL BASIS, THIS WOULD REPRESENT FOR IRAN ALONE ROUGHLY \$2.2
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BILLION IN ADDITIONAL REVENUES.

7. WE FEEL THAT A SINGLE-PRICE SYSTEM MAY BE ON ITS WAY, AS NO ONE CAN LIVE WITH THE PRESENT CONFUSION. THUS WE FEEL THAT IT IS NOW MORE URGENT THAN EVER TO HOLD PRODUCER-CONSUMER TALKS BEFORE POSITIONS ARE HARDENED ON THIS ISSUE AND ON EVEN MORE DIFFICULT ISSUE OF "INDEXATION" OF SINGLE PRICE TO WORLD INFLATION. WE NOTE THAT A CERTAIN INCREASE IN URGENCY OF IRANIAN CALLS FOR SUCH TALKS HAS CREPT INTO LANGUAGE OF GOI OFFICIALS.
HELMS

NOTE BY OC/T: EXDIS CAPTION ADDED PER S/S-O, MR. TWOHIE.

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